

TUESDAY MORNING CORPORATION
RECONCILIATION OF NON-GAAP FINANCIAL MEASURES
(Unaudited)

GAAP Selling, general and administrative expenses to Non-GAAP Adjusted Selling, general and administrative expenses:

The following table reconciles selling, general, and administrative expenses, the most directly comparable GAAP financial measure, to adjusted selling, general, and administrative expenses, a non-GAAP financial measure:

(in thousands)

	<i>Three Months Ended</i>		<i>Six Months Ended</i>	
	<i>December 31,</i>		<i>December 31,</i>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Selling, general, and administrative expenses (GAAP)	\$ 81,053	\$ 84,194	\$ 156,947	\$ 159,984
Non-GAAP adjustments:				
Store reorganization and clean-up	—	(1,125)	—	(1,125)
Compensation	—	(1,542)	(1,554)	(1,686)
Legal, consulting, and recruiting	<u>(244)</u>	<u>(2,682)</u>	<u>(1,083)</u>	<u>(4,031)</u>
Adjusted Selling, general, and administrative expenses (Non-GAAP)	<u>\$ 80,809</u>	<u>\$ 78,845</u>	<u>\$ 154,310</u>	<u>\$ 153,142</u>

GAAP Operating Income/(Loss) to Non-GAAP Adjusted Operating Income:

The following table reconciles operating income/(loss), the most directly comparable GAAP financial measure, to adjusted operating income, a non-GAAP financial measure:

(in thousands)

	<i>Three Months Ended</i>		<i>Six Months Ended</i>	
	<i>December 31,</i>		<i>December 31,</i>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Operating income/(loss) (GAAP)	\$ 18,285	\$ (22,593)	\$ 5,818	\$ (33,477)
Non-GAAP adjustments:				
Adjustment reducing cost of sales:				
Inventory write-down	1,810	41,809	1,810	41,809
Adjustments reducing selling, general and administrative expenses:				
Store reorganization and clean-up	—	1,125	—	1,125
Compensation	—	1,542	1,554	1,686
Legal, consulting, and recruiting	<u>244</u>	<u>2,682</u>	<u>1,083</u>	<u>4,031</u>
Adjusted operating income (Non-GAAP)	<u>\$ 20,339</u>	<u>\$ 24,565</u>	<u>\$ 10,265</u>	<u>\$ 15,174</u>

GAAP Net Income/(Loss) to Non-GAAP Adjusted Net Income:

The following table reconciles net income/(loss) from continuing operations, the most directly comparable GAAP financial measure, to adjusted net income from continuing operations, a non-GAAP financial measure:

(in thousands)

	<i>Three Months Ended December 31,</i>		<i>Six Months Ended December 31,</i>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Net income/(loss) (GAAP)	<u>\$ 17,674</u>	<u>\$ (21,466)</u>	<u>\$ 5,665</u>	<u>\$ (28,427)</u>
Non-GAAP adjustments:				
Inventory write-down, net of tax ⁽¹⁾⁽²⁾	2,146	26,349	2,190	26,511
Store reorganization and clean-up, net of tax ⁽¹⁾⁽²⁾	—	709	—	713
Compensation, net of tax ⁽¹⁾⁽²⁾	—	972	1,880	1,069
Legal, consulting, and recruiting, net of tax ⁽¹⁾⁽²⁾	289	1,690	1,208	2,556
Disposal of systems, net of tax ⁽¹⁾⁽²⁾	—	875	103	880
Deferred tax asset valuation allowance	(772)	6,324	(1,667)	6,324
Adjusted net income (non-GAAP)	<u>\$ 19,337</u>	<u>\$ 15,453</u>	<u>\$ 9,379</u>	<u>\$ 9,626</u>

(1) The effective tax rate utilized in this non-GAAP adjusted net income/(loss) reconciliation is (18.5%) for the three months ended December 31, 2013 and 37.0% for the three months ended December 31, 2012. This rate is inclusive of a deferred tax asset valuation allowance of \$18.1 million as of December 31, 2013 and of \$6.3 million as of December 31, 2012.

(2) The effective tax rate utilized in this non-GAAP adjusted net income/(loss) reconciliation is (21.0%) for the six months ended December 31, 2013 and 36.6% for the six months ended December 31, 2012. This rate is inclusive of a deferred tax asset valuation allowance of \$18.1 million as of December 31, 2013 and of \$6.3 million as of December 31, 2012.

GAAP Net Income/(Loss) Per Share to Non-GAAP Adjusted Net Income Per Share:

The following table reconciles diluted EPS from continuing operations, the most directly comparable GAAP financial measure, to adjusted diluted EPS from continuing operations, a non-GAAP financial measure:

	<i>Three Months Ended December 31,</i>		<i>Six Months Ended December 31,</i>	
	2013	2012	2013	2012
Diluted EPS (GAAP)	\$ 0.41	\$ (0.51)	\$ 0.13	\$ (0.68)
Non-GAAP adjustments:				
Inventory write-down, net of tax ⁽¹⁾⁽²⁾	0.05	0.63	0.06	0.63
Store reorganization and clean-up, net of tax ⁽¹⁾⁽²⁾	—	0.02	—	0.02
Compensation, net of tax ⁽¹⁾⁽²⁾	—	0.02	0.04	0.03
Legal, consulting, and recruiting, net of tax ⁽¹⁾⁽²⁾	0.01	0.04	0.03	0.06
Disposal of systems, net of tax ⁽¹⁾⁽²⁾	—	0.02	—	0.02
Deferred tax asset valuation allowance	(0.02)	0.15	(0.04)	0.15
Adjusted diluted EPS (non-GAAP)	\$ 0.45	\$ 0.37	\$ 0.22	\$ 0.23

- (1) The effective tax rate utilized in this non-GAAP adjusted EPS reconciliation is (18.5%) for the three months ended December 31, 2013 and 37.0% for the three months ended December 31, 2012. This rate is inclusive of a deferred tax asset valuation allowance of \$18.1 million as of December 31, 2013 and of \$6.3 million as of December 31, 2012.
- (2) The effective tax rate utilized in this non-GAAP adjusted EPS reconciliation is (21.0%) for the six months ended December 31, 2013 and 36.6% for the six months ended December 31, 2012. This rate is inclusive of a deferred tax asset valuation allowance of \$18.1 million as of December 31, 2013 and of \$6.3 million as of December 31, 2012.

RESULTS OF OPERATIONS

The following tables set forth certain financial information from our consolidated statements of operations for the second quarter and the six months ended December 31, 2013 and the corresponding periods in 2012. In addition to our reported results, we have also provided adjusted (Non-GAAP) financial information to provide readers with additional information comparing our core results between the second quarter and the six months ended December 31, 2013 and the corresponding periods in 2012.

(in thousands, except for per share data, percentages and ratios)

	Three Months Ended December 31, 2013			Three Months Ended December 31, 2012		
	GAAP	Non-GAAP Adjustments	Adjusted (Non-GAAP)	GAAP	Non-GAAP Adjustments	Adjusted (Non- GAAP)
Net sales	\$ 285,771	—	\$ 285,771	\$ 285,312	—	\$ 285,312
Percent increase from prior year	0.2%	—	0.2%	4.5%	—	4.5%
Comparable store sales increase ⁽¹⁾	3.1%	—	3.1%	5.6%	—	5.6%
Gross profit ⁽²⁾	\$ 99,338	\$ 1,810	\$ 101,148	\$ 61,601	\$ 41,809	\$ 103,410
Selling, general and administrative expenses ⁽²⁾	\$ 81,053	\$ (244)	\$ 80,809	\$ 84,194	\$ (5,349)	\$ 78,845
Operating income/(loss) ⁽³⁾	\$ 18,285	\$ 2,054	\$ 20,339	\$ (22,593)	\$ 47,158	\$ 24,565
Interest income	\$ 11	—	\$ 11	—	—	—
Interest expense	\$ (394)	—	\$ (394)	\$ (486)	—	\$ (486)
Other income, net	\$ 3	—	\$ 3	\$ (1,267)	\$ 1,387	\$ 120
Income tax provision/(benefit)	\$ 231	\$ 391	\$ 622	\$ (2,880)	\$ 11,626	\$ 8,746
Net income/(loss) ⁽³⁾	\$ 17,674	\$ 1,663	\$ 19,337	\$ (21,466)	\$ 36,919	\$ 15,453
Diluted income/(loss) per share ⁽³⁾	\$ 0.41	\$ 0.04	\$ 0.45	\$ (0.51)	\$ 0.88	\$ 0.37
Ratios as a percent of net sales:						
Gross profit	34.8%	0.6%	35.4%	21.6%	14.7%	36.2%
Selling, general and administrative expenses	28.4%	(0.1%)	28.3%	29.5%	(1.9%)	27.6%
Operating income/(loss)	6.4%	0.7%	7.1%	(7.9)%	16.5%	8.6%

(1) Stores are included in the comparable store sales calculation at the beginning of the quarter following the anniversary date of the store opening. A store that relocates within the same geographic market or modifies its available retail space is still considered the same store for purposes of this computation.

(2) See the preceding "Reconciliation of Non-GAAP Financial Measures" section for details on these adjustments. The adjustment to gross profit and the components of the adjustments to selling, general and administrative expenses are set forth in the preceding tables.

(3) See the preceding "Reconciliation of Non-GAAP Financial Measures" section for a discussion of these non-GAAP measures and reconciliation to their most directly comparable GAAP financial measures and further information on their uses and limitations.

(in thousands, except for per share data, percentages and ratios)

	Six Months Ended December 31, 2013			Six Months Ended December 31, 2012		
	GAAP	Non-GAAP Adjustments	Adjusted (Non-GAAP)	GAAP	Non-GAAP Adjustments	Adjusted (Non-GAAP)
Net sales	\$ 469,449	—	\$ 469,449	\$ 458,107	—	\$ 458,107
Percent increase from prior year	2.5%	—	2.5%	3.2%	—	3.2%
Comparable store sales increase ⁽¹⁾	5.4%	—	5.4%	4.0%	—	4.0%
Gross profit ⁽²⁾	\$ 162,765	\$ 1,810	\$ 164,575	\$ 126,507	\$ 41,809	\$ 168,316
Selling, general and administrative expenses ⁽²⁾	\$ 156,947	\$ (2,637)	\$ 154,310	\$ 159,984	\$ (6,842)	\$ 153,142
Operating income/(loss) ⁽³⁾	\$ 5,818	\$ 4,447	\$ 10,265	\$ (33,477)	\$ 48,651	\$ 15,174
Interest income	\$ 15	—	\$ 15	—	—	—
Interest expense	\$ (769)	—	\$ (769)	\$ (908)	—	\$ (908)
Other income, net	\$ 83	—	\$ 83	\$ (1,209)	\$ 1,387	\$ 178
Income tax provision/(benefit)	\$ (518)	\$ 733	\$ 215	\$ (7,167)	\$ 11,985	\$ 4,818
Net income/(loss) ⁽³⁾	\$ 5,665	\$ 3,714	\$ 9,379	\$ (28,427)	\$ 38,053	\$ 9,626
Diluted income/(loss) per share ⁽³⁾	\$ 0.13	\$ 0.09	\$ 0.22	\$ (0.68)	\$ 0.91	\$ 0.23
Ratios as a percent of net sales:						
Gross profit	34.7%	0.4%	35.1%	27.6%	9.1%	36.7%
Selling, general and administrative expenses	33.4%	(0.6%)	32.9%	34.9%	(1.5%)	33.4%
Operating income/(loss)	1.2%	0.9%	2.2%	(7.3)%	10.6%	3.3%

(1) Stores are included in the comparable store sales calculation at the beginning of the quarter following the anniversary date of the store opening. A store that relocates within the same geographic market or modifies its available retail space is still considered the same store for purposes of this computation.

(2) See the preceding “Reconciliation of Non-GAAP Financial Measures” section for details on these adjustments. The adjustment to gross profit and the components of the adjustments to selling, general and administrative expenses are set forth in the preceding tables.

(3) See the preceding “Reconciliation of Non-GAAP Financial Measures” section for a discussion of these non-GAAP measures and reconciliation to their most directly comparable GAAP financial measures and further information on their uses and limitations.